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STATE FOR EAP/CM AND EEB/OMA, TREASURY FOR OASIA

E.O. 12958: N/A
TAGS: ECON EFIN EINV ETRD HK CH
SUBJECT: Hang Seng Falls to Lowest Level in Six Years

¶1. Summary: The Hang Seng Index dropped over 13 percent the week of October 20-24. On the good side, HIBOR fell to just 0.8 percent for overnight but was still 3.6 percent for one month lending, suggesting that the recent HKMA liquidity injection was having only marginal benefits for interbank lending. The press reports that major Hong Kong banks are tightening terms on credit card payments to some very small merchants. These changes appear to be targeted at risky lenders and may be a way for banks to hedge against loan defaults. HKMA warned that banks should continue to exercise sound risk management, despite government deposit guarantees. Hong Kong's inflation rate fell slightly as government subsidies cushioned price increases. End summary.

Hang Seng Index drops 13.3 percent for the week; falls below 13,000

¶2. The Hang Seng Index lost 1142.11 points or 8.3 percent on Friday, following regional markets down, to close at 12618.38; daily trading volume was HKD 56 billion. Compared to last Friday, October 17, the Hang Seng Index lost 13.3 percent or 1935.83 points. HSBC lost 12.5 percent today, closing at HKD 88, the lowest level since Hong Kong was hit by SARS in 2003. The Hang Seng Index has lost 55 percent this year, and almost 60 percent from last year's historic high on October 30. In the month of October alone, the Hang Seng Index has lost 30 percent. HIBOR quoted by Hang Seng Bank at 5:30 pm was 0.8 percent for overnight, 2.0 percent for 1-W, 2.75 percent for 2-W, 3.60 percent for 1-M, 2-M, 3-M and 6-M, all down from October 17 when HIBOR stood at 1.5 percent for overnight, 2.75 percent for 1-W, 3.25 percent for 2-W and 4.1 percent for 1-M, 2-M and 3-M.

Banks Changing Credit Card Payment Terms for Very Small Merchants

¶3. Press reports that some Hong Kong banks (HSBC and Hang Seng are mentioned specifically) have unilaterally changed credit card payment terms for selected very small merchants. Instead of paying merchants within two days, these banks reportedly have extended the repayment period to 60 days for some small beauty salons and travel agents. Both HSBC and Hang Seng have declined to comment. If true, these reports probably reflect a growing concern that these small enterprises will go under without providing already purchased services. Both travel agents and beauty salons in Hong Kong typically require payment in advance for packages or services provided in the future. During difficult economic times, these businesses often go under quickly and without warning. To minimize the chance that banks will be held liable for tickets or services never provided, the banks may be extending the time period for reimbursing the companies. The banks could also be holding these receivables against loan payments in order to minimize the risk if the merchant goes under. This new policy may drive some small merchants out of business, unless they can shift their accounts to another bank. Currently only very small businesses seem to be affected. It is unlikely that larger merchants or those with decent credit histories will be subject to this type of renegotiation.

HKMA Warns on Sound Risk Management

¶4. HKMA Deputy Chief Executive Y.K. Choi told the press today that

the HKMA would not relax its strict supervision of Hong Kong banks. He encouraged banks not to become complacent in their risk management processes following the government's promise of blanket protection for bank deposits. Choi said HKMA has requested all banks to submit weekly reports on high-risk loans. Thursday, October 23, the HKMA injected HKD 3.9 billion (US$ 500 million) into the banking sector as the Hong Kong dollar hit the strong side of the pegged rate, trading at HKD 7.7535/USD. Market sources said in recent weeks there was an indication that some deposits have started to return to Hong Kong; as a result the demand for Hong Kong dollars has been rising. HKMA's market intervention this week was meant to check the rising pegged rate, not to increase liquidity to the banks.

September Inflation Checked by Government Subsidies

¶5. Hong Kong's consumer price index in September was 6.1 percent (net of the effects of the government's one-off relief measures), slightly lower than the 6.3 percent CPI in August. For the first nine months, Hong Kong's consumer price index rose by 5 percent from a year ago. Food prices increased the most, up 14.9 percent from a year ago.